

October 31, 1991

**COORDINATED ISSUE  
SAVINGS AND LOAN INDUSTRY  
VALIDITY OF REGULATIONS SECTION 1.593-6A(b)(5)(vi)**

**Issue:**

Is Treasury Regulations section 1.593-6A(b)(5)(vi) a valid regulation?

**Facts:**

In 1978 the regulations under section 1.593-6A(b)(5) were revised. This revision contained the current provisions which require a recomputation of the bad debt deduction in the event of a NOL carryback.

**Law & Discussion:**

IRC section 593 permits a savings & loan to deduct for tax purposes a reasonable addition to a reserve for bad debts. Section 593(b) provides that this shall include a reasonable addition to the reserve for losses on qualifying real property loans. That section sets forth several alternative methods of calculating the deductible amount. Under the percentage of taxable income method the savings & loan is permitted to deduct a statutory percentage of taxable income. In 1969 the percentage was 60% and gradually decreased to 40% in 1979. The current 8% rate began in 1987.

Section 593(b) also states that "taxable income," for purposes of the bad debt deduction computation, shall be computed by excluding several types of income, including gain arising from the sale of stock and certain dividends. Section 593 does not make any explicit reference to a NOL carried back from a subsequent year or the effect of such NOL on the taxable income computation. Treas. Reg. section 1.593-6A(b)(5)(vii), however, specifically provides that for years beginning after 1977, taxable income under IRC section 593(b) shall be adjusted for a NOL carryback, requiring recomputation of the bad debt deduction. Regulation 1.593-6A(b)(5)(vi), moreover, provides that for years beginning before 1978, such bad debt deduction must similarly be recomputed in the event of a NOL carryback, unless such NOL originates in a year prior to 1979.

IRC section 593(b)(2) provides for a bad debt computation based on "taxable income." Regulations section 1.593-6A(b)(5) provides exceptions to the regular definition of taxable income but neither section provides a definition of taxable income. Section 63 of the IRC provides the necessary definition. It defines "taxable income" as gross

income minus the deductions allowed by Chapter I of the Internal Revenue Code, which includes the NOL deduction set forth in IRC section 172. Congress made a comprehensive revision to section 1.593-6A(b)(5) in 1969 (which included an exhaustive list of exceptions to taxable income for section 593 purposes) but did not include a provision for NOL's. The revised regulations published in 1978 which call for a recomputation of the bad debt deduction in the event of a NOL carryback are therefore consistent with the Code and the intent of Congress.

**Conclusion:**

Regulation section 1.593-6A(b)(5)(vi) is a valid regulation. Accordingly, if there is an NOL carryback originating after 1978, the savings & loan must adjust taxable income by such NOL carryback and recompute the bad debt deduction for the carryback year based upon the adjusted taxable income.